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SEMANTICS AND THE STOCK MARKET

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SEMANTICS AND THE STOCK MARKET

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INTRODUCTION

The life of the business corporation in theory is perpetual. Man, on the other hand, is "born in the shadow of the grave." Certainty of his life span is unknown, but certainty that it is a span and not perpetuity is known. Man has only so many years of economic productivity in which to make his financial mistakes, learn his lessons, and then to postulate and carry out what will hopefully be a rational approach to his future economic well-being. The corporation, in theory, can make its mistakes, learn its lessons, plan for future years, and then engage in the same cycle ad infinitum.

From the standpoint of time, the burden of proper financial management is more on man and his personal finances than it is on man and corporate finances.

The stock market has an understandable allure for the man who desires to funnel his productive years' income into investments promising future financial security. Funds invested in stocks possess liquidity (except, perhaps, some unlisted stocks), offer a potential for capital gain or dividend income, or both, permit the investor to know, almost to the penny, the exact value of his investments at any time and, if the investor is successful, provide a hedge against inflation. But all these benefits are counterbalanced by the risks inherent in stock ownership. The investor may well find that his investments are providing a flow of funds, as he hoped, but in the wrong direction.

The field of literature is not remiss in providing man with an abundance of printed matter designed to ease his way quickly into the mysteries of the stock market. The usual treatise on the stock market is largely concerned with either the mechanics of the market, methods of "making money" on the market, defining investor objectives, presenting investment plans, discussing the principles of stock investing, or combinations of any of these.

These approaches are roughly analogous to the man who is taught the formula for computing the current ratio of corporations, but has not been taught nor does he understand why the "things" classified as assets and liabilities mean different things to different concerns and are valued differently by different concerns. In short, he understands and has memorized the formula but he does not know what the formula means.

Investors live in a world of words peculiar to the stock market and, although most of them understand these words and how and when to use them, their glibness does not bring about knowledge of how these seemingly innocent words affect them and what they do in the market.

It is my thesis that semantics, and particularly the general semantics of Korzybski, provides a "way of thinking" about the stock market which is basic to success in the market. I do not believe that everyone who is successful in the market has consciously thought about or consciously applied this semantic approach or that they even know what semantics and general semantics are; but I do believe that truly successful stock investors have either consciously or intuitively applied this way of thinking.

Two examples of this applied way of thinking are found in Bernard Baruch's Autobiography¹ and G. M. Loeb's, The Battle for Investment Survival.² Although neither of these highly successful investors uses the word "semantics" in any of its forms or derivations, both their books indicate an intuitive, if not conscious, semantical approach to investing.

It is not contended that knowledge and understanding of the semantics of the stock market will necessarily make the unsuccessful stock investor a successful investor. If this were actually the case, the writer would be too busy with his investments to write this paper. However this approach will provide the basis for a more rational approach to the stock market than is otherwise possible.

The problems of the stock investor are numerous. From the standpoint of semantics, particularly general semantics, the writer contends that the major problems are five:

1. Understanding the symbology of the market.
2. Emotional reactions to words such as speculator and technician.
3. Obtaining and understanding market information.
4. Recognizing the nature of forecasts and their limitations.
5. Assessing success in the stock market.

¹Bernard M. Baruch, Baruch: My Own Story (New York: Holt, Rinehart and Winston, 1957).

²Gerald M. Loeb, The Battle for Investment Survival (New York: Hurry House Publishers, 1953).

It is to these five problem areas that this paper is addressed. The point of view is broadly that of the field of semantics but more particularly general semantics.

CHAPTER I

THE SYMBOLISM OF THE STOCK MARKET

. . . the patriotic archbishop of Canterbury, found it advisable _____,"

"Found what?" said the Duck.

"Found it," the Mouse replied, rather crossly: "of course you know what 'it' means."

"I know what 'it' means well enough, when I find a thing," said the Duck: "it's generally a frog, or a worm."¹

--Lewis Carroll

What Is the Stock Market?

The stock market is an inimitable place. It does not recognize differences of age, color, race, or creed. It does not care if one is an atheist, a left-winger, or a right-winger. Whether illiterate, a do-gooder, a no-gooder, a symbol of virtue or dissipation—the market will welcome all with open arms. The stock market, in short, personifies the democratic process.

But what is the stock market?

Dice and Eiteman, in their definitive book, The Stock Market,² devoted 449 pages to the stock market without defining the term "stock market" in their text. Their preface, however, defined the "stock market" as an

¹Alice in Wonderland.

²Charles A. Dice and Wilford J. Eiteman, The Stock Market (New York: McGraw-Hill Book Company, Inc., 1952).

institution that:

. . . has been developed to make the ownership of stocks safer and more convenient and to put the business of investment on a higher plane of intelligence and honesty.³

This is a strangely antiseptic definition, completely devoid of the dynamics of the human beings who buy and sell stocks and provide the services that make the "market." This definition ignores the emotions, rumors, speculation and dramatic price movements common to the buying and selling of stocks, and certainly is not descriptive of what the gallery visitor to the New York Stock Exchange observes on the floor below him.

But these objections to the stated definition are personal and reflect the inadequacy of a definition-description to agree with one's mental picture of the "stock market." To the writer, the "stock market" is the broker, the bookkeeper, the floor trader, the specialist, the investor, Wall Street, the over-the-counter dealer. It is all of these things and more. It is the analyst, the advisory letter writer, the sophisticate who purchased eight shares of stock in 1951 and brags that he "has never lost money in the market." The "market" includes the rationale of the investor who watches the market price of his stock drop \$25 a share in five months and consoles himself with the thought that, after all, it is a quality stock and besides, look at the \$3.60 annual dividend it pays.

Although this mental concept of the "stock market" may be adequate for the writer's purposes, it may not be so for others. Perhaps to the janitor the "stock market" represents the littered trading floor of the New York Stock Exchange; to the broker's bookkeeper it is "that place" where, if

³Ibid., p. v.

the volume of trading gets too high, "they" make him stay after five o'clock to close out the accounts; to the lithographer it is that place where new issues of stock mean new business printing stock certificates.

To Bernard Baruch, the "stock market" takes the form of a "total barometer for our civilization" as the prices of stocks "are affected by literally anything and everything that happens in our world."⁴ Jacob Kamm looks upon the "stock market" as some form of an All-American hobby shop:

Every American ought to take advantage of this opportunity of stock ownership. It can be not only a pleasant experience but also a profitable hobby.⁵

But to G. M. Loeb the "stock market" must be an arena, as inferred from the title of his book, The Battle For Investment Survival.

Who is right? And by what standard do we determine "right"? The use of a dictionary to settle our problem is of limited value because the writing of a dictionary

. . . is not a task of setting up authoritative statements about the "true meanings" of words, but a task of recording, to the best of one's ability, what various words have meant to the authors in the distant or immediate past. The writer of a dictionary is a historian, not a lawgiver.⁶

We cannot find the "stock market" to photograph it, or to point to it, in the hope of identifying it to the degree that we can say what it "is."

⁴Baruch, p. 84.

⁵Jacob O. Kamm, Making Profits in the Stock Market (New York: The World Publishing Company, 1952), p. 152.

⁶Samuel I. Hayakawa, Language in Thought and Action (New York: Harcourt, Brace and Company, 1949), p. 55.

At this point in our search for a definition of the "stock market", however, we can identify three "things":

1. The term "stock market."
2. The undefined reality of what the "stock market" is.
3. The mental concept of what the term "stock market" means to various individuals.

We can also define the relationship that exists between these three "things":

The "stock market" is a term which stands for, or represents, the mental concepts of what each user of the term conceives the reality of the "stock market" to be.

Thus, the term "stock market" is a symbol. It is a symbol of reality as that reality appears to each user of the term "stock market."⁷

The words "stock market" mean nothing by themselves; only at such a time as when they are used together do they stand for anything; only at that time do they have meaning.⁸ And the only meaning the symbol "stock market" can have is the meaning attached to it by the mind of the user.⁹ Therefore, the only direct relationship that exists between symbol, mental concept, and reality, is that between symbol and mental concept—for symbols provide the means for communicating thoughts about reality and not reality itself.¹⁰

⁷Alfred Korzybski, Science and Sanity (3d ed.; Lakeville, Conn.: The International Non-Aristotelian Library Publishing Company, 1948), pp. 76-84; also see Hayakawa, pp. 24-28.

⁸Charles K. Ogden and I. A. Richards, The Meaning of Meaning (8th ed.; New York: Harcourt, Brace and Company, 1948), pp. 9-10.

⁹Frank Nesbit, Language, Meaning and Reality (New York: Exposition Press, Inc., 1955), p. 165.

¹⁰Ogden and Richards, p. 9.

Each individual using a symbol is uniquely free "to manufacture and manipulate and assign values" to the symbol as he pleases.¹¹ Whether or not the values assigned to the symbol "stock market" are adequate depends solely upon the purpose for which the symbol "stock market" is used and not on the intrinsic worth of the "values" themselves. Thus, if the Stock Exchange janitor's view that the "stock market" is "the littered floor of the New York Stock Exchange" is adequate for his purposes, then his meaning assigned to the symbol "stock market" is as valid as that assigned by Baruch.¹²

Thus, all the different meanings of "stock market" as discussed are correct to the degree that they adequately reflect the individual's concept of reality. But conflict between different meanings and the individuals using these meanings is inevitable when the symbol is identified as the thing symbolized. In other words, when individuals fail to recognize the symbolic process, when they think that their meaning is the only "correct" meaning, the resultant can range from semantic arguments to war.

We can never know all there is to know about any "reality," that is, it is impossible to know everything about anything.¹³ Therefore, if all the different meanings of the "stock market" were added together, we would still know only a fraction of the total of the reality of the "stock market." In short, we can never fully define "stock market." If man contends that he

¹¹ Hayakawa, p. 25.

¹² Charles W. Morris, Signs, Language, and Behavior (New York: George Braziller, Inc., 1955), p. 93.

¹³ Cassius J. Keyser, Mole Philosophy and Other Essays (New York: E. P. Dutton & Co., 1927), p. 132; H. A. Overstreet, The Mature Mind (New York: W. W. Norton and Company, Inc., 1949), p. 46; Sidney Ratner, "Presupposition and Objectivity in History," Philosophy of Science, October, 1940, p. 504; and George Santayana, Obiter Scripta (New York: Charles Scribner's Sons, 1936), ed. Justus Buchler and Benjamin Schwartz, p. 132.

has fully defined "stock market," or any other term, then, according to Kayser:

. . . either he is a performer of logical miracles or he is an ass; and, as you know, logical miracles are impossible.¹⁴

Even if we assume that man can perform logical miracles, that which we did know at any one moment of time would not be the same at the next moment because reality would have changed and our "dated" description of reality would no longer be accurate. Heraclitus, the Greek, contended that it was impossible to step in the same river twice. In the same way of thinking, it is impossible to say what the "stock market" is, as it is not the static object inferred from Dice and Eiteman's definition, but rather it is a dynamic process.

The Investor and the Symbol

To the investor, what merit is there in knowing that the "stock market" is a symbol? Perhaps of greatest importance is the realization that in using the symbol, or any other of the symbols of the stock market, we are not talking about reality. This knowledge permits the investor to assess statements about the stock market as generalizations and as unreal, imperfect statements. For example, when a market commentator [imaginary] says: "The stock market staged an advance accompanied by heavy volume," we know that some stocks dropped in price, some stocks were not traded that period, and the trading volume on some stocks probably decreased. We know that what the commentator was actually saying was something like this:

¹⁴ Cassius J. Keyser, Mathematical Philosophy (New York: E. P. Dutton, 1922), p. 152.

One or more of the 30 stocks comprising the Dow-Jones Industrial Average advanced sufficiently in price to offset the market price movement of the remaining stocks comprising this Index so the net result was a higher Dow-Jones Industrial Average than for the previous day. Coincidentally, the volume of the day's trading in all of the stocks listed on the New York Stock Exchange was heavy in the sense that the number of shares traded was greater than the number of shares traded on the previous day.

With this look at reality, we would not be surprised or confused to note that the Standard & Poor's Index dropped, that only one of the 30 stocks used in the Dow-Jones Industrial Average advanced, that the other 29 stocks in this Index closed at or below their previous closing price, and that the increase in trading volume was due to increased activity in stocks other than those included in the Dow-Jones Industrials. We also know that nothing has been said about the stocks traded on the other 16 stock exchanges in the United States, the stocks traded on the over-the-counter market, or stocks traded on the foreign exchanges. In short, we have not made the mistake of confusing the commentator's symbol with the "thing" symbolized.

We further know that the symbol "stock market" is not what we buy when we buy stock. The symbol "stock market" as represented by the averages or Indexes may go up, down, or hold relatively steady. But our stock, which is not the symbol, may either move contrary to the "market," with the "market," or not move at all.

The Abstraction of the Stock Market

In symbolization there is a relationship between (1) the mind, which we have already discovered attaches meaning to that which acts as a

symbol; (2) the symbol itself; and, (3) the process, thing, or object, called "reality" or referent, meant by the symbol.¹⁵

Thus far the "stock market," as a symbol, has been "lifted out" of the total complex of our social structure and considered as an entity independent of other social activity. In actuality, the referent, "stock market," is but one aspect of social activity and cannot exist as a separate entity but only as an interrelated and interconnected part of the whole of society. But, if we are to avoid hopeless confusion, we find this "lifting out," or abstracting, of the "stock market" from the whole of its environment is a necessity. Although it is the nature of our thinking process, and a function of symbolization, to abstract a part from the whole, what we must recognize, as previously pointed out, is that the symbol is not that which is symbolized.¹⁶

Each individual user of the symbol "stock market" ascribes certain characteristics of his knowledge of the reality of the "stock market" to the symbol "stock market." The characteristics that are ascribed by some process of "knowing," "feeling," or "interest," etc., are those which are useful or meaningful to the individual; they do not, and cannot, include all of the characteristics of the reality of the "stock market."¹⁷ The symbol, "stock market," is recognized as an abstraction, and as such it is not the "thing in itself" but "an interaction between our nervous systems . . . and something outside them."¹⁸

This act of abstracting is an indispensable convenience for communicating. If we were required to communicate on the basis of specific

¹⁵Nesbit, p. 165.

¹⁶Ibid., p. 101.

¹⁷Korzybski, p. 414.

¹⁸Hayakawa, p. 167.

meanings rather than on the basis of general terms [symbols] at higher levels of abstraction, our everyday world would become too complicated, verbally, to permit other than the accomplishment of the most rudimentary processes.

The freedom we have to abstract our symbol contexts in a manner most meaningful to us is the same freedom others possess to abstract their own meaningful symbol contexts. Each individual, then, builds his own framework of reference which has an existence apart from the frameworks of other persons. When we communicate, we share our frameworks of reference. But we should feel some constraint in our communication process when we realize the differences that exist between our individual frameworks of reference. For "there are as many different symbol contexts as there are different persons in the world . . ."¹⁹

This failure to recognize that each individual has his own framework of reference leads to difficulty and, in some cases, to highly emotional reactions to symbols. It is perfectly normal for humans to conclude, upon reading or hearing a communication, that the speaker or writer is referring to what they would be referring to if the positions were reversed.²⁰ But this conclusion is rarely justified, as no two individuals have identical experiences in life from which to build their contexts.

The words "speculator" and "investor" provide us with perfect examples of confusion between different frameworks of reference and the emotional reaction resulting from this confusion, which is the subject of chapter II.

¹⁹Hugh R. Walpole, Semantics (New York: Norton & Co., Inc., 1941), p. 114.

²⁰Ogden and Richards, p. 15.

CHAPTER II

INVESTOR AND SPECULATOR

When as a young and unknown man I started to be successful, I was referred to as a gambler. My operations increased in scope and volume. Then I was known as a speculator. The sphere of my activities continued to expand and presently I was known as a banker. Actually I had been doing the same thing all the time.¹

--Sir Ernest Cassell

The word "investor" was used in chapter I in its broad, all-inclusive sense. That is, an investor is one who makes investments. To define "investor," then, we must first have an acceptable definition of "investment."

To Clendenin, an investment "is any asset or property right acquired or held for the purpose of conserving capital or earning an income."² Dowrie and Fuller were more optimistic in their definition of an investment in that they were not concerned with the minimum aim of preserving capital. To them an investment "may be defined broadly as the employment of capital with the aim of producing a gain in the shape of income or appreciation in value or both . . ."³ A synthesis of these two definitions would be:

¹Attributed to Sir Ernest Cassell, the private banker to King Edward VII; quoted from Baruch, p. 247.

²John C. Clendenin, Introduction to Investments (3d ed.; New York: McGraw-Hill Book Company, Inc., 1960), p. 2.

³George W. Dowrie and Douglas R. Fuller, Investments (2d ed.; New York: John Wiley & Sons, Inc., 1950), p. 34.

An investment is the employment of capital for the purpose of preserving capital, earning an income, or gaining capital appreciation.

It is the writer's opinion that the act of preserving one's capital is quite an accomplishment, in periods of dollar depreciation, and, therefore worthy of being included as an aim in an investment program.

With this definition of investments, the investor has a wide range of opportunities for employment of his capital. Savings accounts, life insurance,⁴ real estate, business equities,⁵ corporate stocks, bonds, mortgages, etc., are all investments within the meaning of the definition.

However, when the word "investor" is applied exclusively to the purchase and sale of stocks, it is common to find that "investor" assumes a connotation different from that of "investor" in the broad, generic sense. This change in sense or meaning, according to the use of the word, is a common event in the English language. The normality of such a change is well stated by Welby: "There is, strictly speaking, no such thing as the sense of a word, but only the sense in which it is used."⁶

When an individual, seeking an opportunity for capital investment, enters the world of the stock market, he finds that he cannot be "just" an investor in the general sense of the word. He must classify himself or be classified as either an investor or a speculator. He cannot be both, nor can he be in-between. He is enjoined to clearly draw a line between being

⁴Excluding term insurance.

⁵Proprietorships and partnerships.

⁶V. Welby, What is Meaning? (London: Macmillan & Co., 1903), p. 5.

an investor or a speculator.⁷ On the one hand he is told that the only safe approach to stock investing is that of the speculator,⁸ while on the other hand he is told that "extensive speculation is not profitable."⁹ As the individual reads more of the literature, he finds sources stating that only investors invest in investments and that there is something good and sound about this type of individual and his method of operations in the stock market.¹⁰ In contrast, the speculator speculates in speculations and this connotes a parasitical activity which is morally wrong.¹¹

Why is it that an individual must be either an investor or a speculator, and why is the investor "good" and the speculator "bad"? To answer the former, the clock will have to be turned back 23 centuries; for the latter, we shall have to invade the world of the "pooh-poohians."

In spite of the dangers of definition, what differentiates the investor from the speculator? Since a speculator engages in making speculations and an investor in making investments, the point of differentiation must be that between speculation and investment. A succinct expression of this difference was given by Dowrie and Fuller in Investments:

In popular usage, the extent to which a security operation is held to be a speculation and not an investment depends primarily on the degree of risk which is believed to have been assumed¹²

⁷Roger Bridwell, "Investor or Speculator? Line Between the Two Must Be Clearly Drawn," Barron's, n.d., 1953.

⁸Loeb, pp. 18-21

⁹Clendenin, p. 3.

¹⁰Lewis D. Gilbert, Dividends and Democracy (Larchmont, New York: American Research Council, 1956), p. 72.

¹¹Dowrie and Fuller, p. 9.

¹²Ibid.

By restricting the definition to popular usage, a speculator can be said to be one who knowingly assumes a high degree of risk in his selection of stock, while an investor is one who selects stock on the basis of assuming minimum risk.

The Either-Or Dichotomy

Some 2300 years ago, Aristotle advanced what to him were the three basic laws of thought of the people of his time. These were the laws of identity, of the excluded middle, and of non-contradiction. Expressed in other terms, his laws can be stated as:

A is A.

Everything must be A or non-A.

Nothing can be both A and non-A.

These generalizations of Aristotle were accepted by his followers as laws of nature and, as such, not subject to revision. In short, his laws were taken as Truth in an A is A sense. Since they were Truth, any modifications of these laws would be non-Truths. Consequently, these laws were continued by the time-binding process¹³ of man as a system of doctrine and as a social structure. This Aristotelian system and social structure fostered a two-valued structure of orientation, i.e., an either-or dichotomy. Something is either true or false, right or wrong, black or white; there is no in-between, no shade of gray.¹⁴ As John Dewey put it:

¹³The process of passing thought, information, and knowledge from one generation to another. See Alfred Korzybski, Manhood of Humanity (New York: E. P. Dutton & Company, 1921), pp. 59-60.

¹⁴Wendell Johnson, People in Quandries (New York: Harper & Brothers, 1946), pp. 6-10.

Mankind likes to think in terms of extreme opposites. It is given to formulating its beliefs in terms of Either-Ors, between which it recognizes no intermediate possibilities.¹⁵

Not only is the two-valued structure of our thinking process firmly rooted in our culture, but our acceptance and continued use of this way of thinking is further strengthened by what Harry and Bonaro Overstreet stated is our "tendency to oversimplify problems and to demand that others oversimplify them."¹⁶ Oversimplification, according to the Overstreets, expresses itself,

. . . as a kind of debate-minded tendency to think of problems as two-sided rather than many-sided, so that we ask people to choose sides rather than explore possibilities; . . .¹⁷

The Aristotelian either-or dichotomy produces the following "laws" when applied to the investor-speculator in the stock market:

Law of identity;

A speculator is a speculator.

or

An investor is an investor.

Law of the excluded middle;

All buyers and sellers of stock must be either a speculator or an investor.

Law of non-contradiction:

No buyer and seller of stock can be both a speculator and an investor.

¹⁵ John Dewey, Experience and Education (New York: The Macmillan Company, 1938), p. 1.

¹⁶ Harry and Bonaro Overstreet, The Mind Alive (New York: W. W. Norton & Company, Inc., 1954), p. 213.

¹⁷ Ibid.

Should the proper approach to stock market operations be two-valued in keeping with these laws, we suffer no disillusionment with our cultural background in that we do not have to invalidate the ancient laws of Aristotle, nor do we have to cease in our application of the simplest two-sided approach to our investment problems. But if the approach to investing (in its general sense) is many-sided then we must discard the structure of the Aristotelian system and redirect our approach to the investment problem from that of the oversimplified two-sided approach to the complex approach of including the "excluded middle." Not to do so would make our approach to the stock market hopeless, because "we cannot hope to grasp a multivalued event with a two-valued tool."¹⁸

This discussion logically leads us to consider some objections to the either-or dichotomy of the Aristotelian system. But before departing this section, we must acknowledge that the division of general investors into the either-or world of investor-speculator has its roots firmly imbedded in our cultural background; it did not "just happen." We must also recognize that acceptance of this two-sided orientation has been further enhanced, as pointed out by the Overstreets, by our tendency to oversimplify.

The Non-Aristotelian Approach

Irving Lee emphatically dismissed the either-or dichotomy of Aristotle with his statement that the "two-valued orientation is obviously not similar structurally to the world of objects, happenings, people, feelings, etc."¹⁹ The founder of the non-Aristotelian system of general

¹⁸ Stuart Chase, Power of Words (New York: Harcourt, Brace and Company, 1954), p. 190.

¹⁹ Irving J. Lee, Language Habits in Human Affairs (New York: Harper & Brothers, 1941), p. 108.

semantics, Alfred Korzybski, pointed out that the "facts of experience" are infinitely multi-valued.²⁰ These thoughts of Lee and Korzybski are difficult to accept, initially, because they violate the usual way of thinking—we dislike to have a concept, recognized for some 2300 years, challenged.

In arguing against the non-Aristotelian approach of Lee and Korzybski, we can use as our basis the everyday observation that people are either male or female. On close examination, however, we find that even this apparently safe dichotomy is not true to nature. Kenneth Keyes illustrated the fallaciousness of this two-sided approach by pointing out that the female has glands that produce male hormones and excrete 70 percent as many male hormones as the male; that the male has glands that produce female hormones and excrete 40 percent as many female hormones as the female. In the abnormal realm of nature, Keyes pointed out that there are about fifty recorded cases of true hermaphrodites.²¹ But no medical or chemical proof is really needed that many of the characteristics of one sex are found in the other. Early in life we recognize the shades of gray between the either-or extremes by classifying some boys as "sissies" and some girls as "tomboys."

Certainly there are some real life facts that are either-or; but not to the extent that careless thinking would lead us to believe. Careful thinking will open many possibilities of including the middle where it has previously been excluded. This is particularly evident when we consider a class of "things." In examining a class, we should bear in mind the fact that a class is comprised of multi-valued items; each item differs from the other in a matter of degree.²²

²⁰For examples, see Korzybski, Science and Sanity. p. 561.

²¹Kenneth S. Keyes, Jr., How to Develop Your Thinking Ability (New York: McGraw-Hill Book Company, Inc., 1950), pp. 61-63.

²²Ibid., pp. 55-72.

But let us return to our process of abstracting previously discussed in chapter I as a way of examining the multivalued approach to a class. When we classify "things" we abstract characteristics that are similar and ignore characteristics that are different.²³ For example, we classify certain animals according to common characteristics and label the class "dog." But all of the characteristics of the Chihuahua, for example, are not the same as all of the characteristics of the St. Bernard; yet both are dogs. Further, in the class of St. Bernards, no particular St. Bernard has all of the characteristics of any other particular St. Bernard. Continuing, a specific St. Bernard, at birth, does not possess all of the characteristics of the same St. Bernard at five years of age. Thus, there are variations between the items within a class and variations within a specific item according to time.

To keep this multivalued, non-Aristotelian concept in mind as an aid to clear thinking, Korzybski recommends using certain working devices which he calls Indexes, Dates, and Etc.²⁴ "Index" numbers are used to separate specifics from generalizations; they allocate a characteristic to an individual rather than to a class containing the individual. "Dates" indicate a change of characteristic with passage of time.

The Korzybskian Index-approach to our general class of investors with respect to their willingness to accept risk would be something like this: Individuals within the total class of stock investors possess varying degrees of willingness to assume risk. Therefore, one cannot say that all

²³See chapter I.

²⁴Korzybski, Science and Sanity, pp. xxxiii-xxxv; these pages give an introductory treatment of Korzybski's three working devices: Indexes, Dates, and Etc. (The device of Etc. will not be discussed.)

investors take unusual risk, nor that all strive for minimum risk; nor would it be proper to say that all investors can be grouped into either extreme, for one extreme shades imperceptibly into the other. To indicate this differentiation between investor characteristics, Index numbers will now be assigned to the word "investor" when speaking of a particular investor. Thus, investor₁ is a specific investor, within the total group of investors, with his own specific characteristics which are different, to some degree, from all other investors. Investor₁, then, is not the same as investor₂. If all investors were arrayed in descending order according to the degree to which they were willing to accept risk in their investments, they would range from No. 1 to No. 15,000,000 (based on an estimate of 15,000,000 stock market investors at the close of 1961).²⁵ Investor₁ would be at the extreme of "willingness to assume risk" end of the array; investor_{15,000,000} would be at the other extreme end of the array, i.e., complete unwillingness to assume risk. With the Index number concept in mind, the absurdity of saying that "stock investors are speculating to an excessive degree" is readily apparent. This statement may well be true of investor₁ and those investors arrayed in proximity to him, but it would be manifestly untrue of investor_{15,000,000} and the investors in proximity to him. It would be equally absurd to say that all investors are either speculators or investors. Investor_{7,500,000} and a few million other investors would probably object to such an arbitrary classification.

There are times, however, when the entire class of investors must or should be referred to collectively. Since reference will be made to the

²⁵Merrill Lynch, Pierce, Fenner & Smith, Inc., Annual Report: 1961, (1962), p. 2.

general class and not to a particular investor or group of investors within the total class, the Index "n" will be used to indicate all investors.

Investor_n includes Investor₁, investor₂, investor₃, . . . investor_{15,000,000}.

Obviously, the assigning of Index numbers is a mental process. This process has great use in making sense out of the vague generalities which all too often are associated with the stock market. An excellent example is found in the following statement made by Joseph Livingston before the Senate Committee on Banking and Currency:

People are no longer buying for income alone, but for capital appreciation. They are not investors; they are speculators.²⁶

In terms of Index numbers, Mr. Livingston said: People_n are no longer However, the reader must decode this meaningless statement by changing the generalization of Mr. Livingston to the more accurate: People_{some} are no longer Perhaps people_{some} was a majority of people_n; but assuredly people_{some} was not people_n.

The non-Aristotelian continues his rebellion by recognizing that the characteristics of an individual are never at rest but change with the passage of time. As Max Born said, "It is odd to think that there is a word for something which, strictly speaking, does not exist, namely "rest."²⁷ Therefore, not only is investor₁ not investor₂ nor investor_n with respect to his speculative approach to the market, but investor₁ of 1929 was not necessarily investor₁ of 1933. In other words, the degree of willingness of our

²⁶ U.S., Congress, Senate, Committee on Banking and Currency, Stock Market Study; Report No. 376, 84th Cong., 1st Sess., May 26, 1955, p. 4.

²⁷ Max Born, The Restless Universe (New York: Harper & Brothers, 1936), p. 1.

extreme risk-taker, investor₁, to assume risk in 1929 was probably not the same as his degree of willingness to assume risk in 1933. We must "date" this same investor to denote his change in a particular characteristic:

Investor₁₉₂₉ is not the same as investor₁₉₃₃.

To summarize indexing and dating: When we speak of investors_n, we do not fall into the semantic trap of confusing investor₁ with investor_{13,745}; nor do we make the error of saying that investor₁₉₆₂ is suffering from the same speculative mania as investor₁₉₂₉.

The practical advantage to the investor with the non-Aristotelian viewpoint is the flexibility of his approach to the risks of the stock market. He recognizes that economic conditions, stock market conditions, investor_n emotions, etc., are dynamic and are constantly ranging from one extreme to another. Within the limits of his attributes, being free from the constraints of the Aristotelian dichotomy, he is able to shift his investment philosophy from conservative to speculative by using all or any of the in-between shades of gray rather than jumping erratically from one extreme to another. With rare exceptions, he holds both speculative and conservative stocks, in varying proportions according to "the times." But he is never a rigidly "pure" speculator or a "pure" conservative.

Why Speculators Are Bad

In Semantics, Walpole described the "pooh-pooh" and "bow-wow" theories of speech origin which were advanced toward the middle of the 19th century.²⁸ The "pooh-pooh" school of thought held that man's first speech consisted of words which were musical accompaniments to man's feelings.

²⁸ Walpole, chapter 2, pp. 38-62.

According to Walpole:

When one has a feeling of disgust or contempt one is apt, to take Darwin's example, "to blow out of the mouth or nostrils, and this produces sounds like pooch or pish." So these words would be the names of feelings or emotions, and such feelings would have labels that fitted very well for the good reason that feeling and label both came from the same physiological source.²⁹

The "bow-wow" theorists maintained, for example, that man heard a dog barking and, in imitation, barked himself. This bark of man became a word which to early man meant "bark" or perhaps "dog" or, more likely, either or both.

During this period of time, of course, there were many other theories of speech origin. The two herein described were singled out by Walpole as illustrating two different motives for using language. The "bow-wowian" talks about something which exists; the "pooch-poochian" expresses his own feelings. Disregarding the validity of either of these two theories, Walpole pointed out that they provide examples of two different functions of language. He refers to these two functions as referential, which is "bow-wow," and emotive, which is "pooch-pooch." According to Walpole:

Referential language refers to objects or actions or situations which can be pointed to or described, and statements which may be verified or disproved by the other fellow. Emotive language expresses the speaker's feelings, and aims at stirring those of the hearer³⁰

²⁹Ibid., p. 39.

³⁰Ibid., p. 40.

Thus, if a communication transmitter wants to evoke a pleasurable feeling or emotion, or desires to indicate approval of an event or thing, he will use "good" words. For the opposite effect he will use "bad" words. As an example, consider some of the emotive words used during a labor strike:

"Good" word: "Loyal" (employee)

"Bad" word: "Scab"

Company approval of the employee who remains on the job during a strike is implied by referring to him as a "loyal employee." As to members of the labor union out on strike, disapproval of the same employee is indicated by the emotional reference to "that scab."³¹

Both the "good" and the "bad" words applied to the nonstriking employee were evaluated as such because of the context of the situation within which they were used. In some instances, however, emotional reaction to a word becomes so strong that the word is "good" or "bad" without regard to its context. A striking example of this was given by Stuart Chase when he related the following case:

A superpatriotic organization proposed in 1953 to exclude the phrase "little red schoolhouse" from discussions of American education. The word "red" ignited the superpatriots, who gave it a quite irrelevant political meaning.³²

To this unnamed organization, the symbol "red" was bad, regardless of context.

³¹William Exton, Jr., "Semantics of Employee Relations," Effective Communication on the Job, ed. M. Joseph Dooker (New York: American Management Association, 1956), p. 70.

³²Chase, pp. 166-167.

Even more pathological is the emotional response to a single word—a word standing without context. So strong is the tendency in our culture to react to emotive language that "practically anyone . . . reacts more or less profoundly to isolated words."³³ The communication receiver does not need the context of a "pooh-pooh" word; so strong is his reaction that he can evaluate and react emotionally to the word as it stands by itself:

Psychologists have developed an instrument which they call a psychogalvanometer, and they use it to record changes in electrical skin potential. Records taken by this instrument show that it is very common, even for so-called educated people, to undergo changes in electrical skin potential in response to hearing or reading isolated words such as mother, blood, love, blue, etc.³⁴

Given the emotional reaction to certain words, how does a word become "bad" or "good"? One can hypothesize that word reactions are largely the results of an individual's inherited semantic environment and his relationships or experiences with "things." Inherited semantic environment means that a word may be "bad" because "authority" says it is bad and not because the individual has had experience with that which is supposed to be "bad."

Initially, the child inherits the evaluative orthodoxy of his parents. As the Overstreets pointed out, adults with their fixed "mental and emotional lodging within religious, political, and economical orthodoxies . . . " stifle the curiosity and wonder of their children by pushing them into the same fixed loyalties of their parents.³⁵ Certain "things" not

³³Johnson, p. 261.

³⁴Ibid.

³⁵Harry and Bonaro Overstreet, pp. 212-213.

yet experienced, the child learns to identify as being bad; others, as being good. And the child soon recognizes, as Lee put it, "that words go with or reflect attitudes or feelings."³⁶ The child sees a dog for the first time; the mother, who was once bitten by a dog, says, "Dog -- Bad!" The child, old enough to have learned what "bad" means, now recognizes its synonym—"dog." Unless by experience the child learns that the characteristics of dog₁ that bit his mother are not the characteristics of dog_n, the natural result would be the child's yelling, "You dog!" at someone or some thing to indicate his disapproval of him or it. The child, in short, is reacting to the symbol and not the thing symbolized.

An interesting example of how experience can provoke emotional reactions to words, to the point of adopting the "ostrich sticking his head in the ground" approach, was given by John Galbraith. In discussing the business cycle, Galbraith pointed out that the word "crisis" was normally employed in the last century to indicate "bad times." But, as Galbraith further pointed out, the word became "bad" and caused the following word changes:

With time, however, this [crisis] acquired the connotation of the misfortune it described. And Marx's reference to the "capitalistic crisis" gave the word an ominous sound. The word panic, which was a partial synonym a half century ago was no more reassuring. As a result, the word depression was gradually brought into use. This had a softer tone; it implied a yielding of the fabric of business activity and not a crashing fall. During the Great Depression the word depression acquired from the event it described an even more unsatisfactory connotation. Therefore the word recession was substituted to connote an unfearsome fall in business activity. But this term eventually acquired a foreboding quality and the recession of 1953-54 was widely characterized as a rolling readjustment. Should we have a really serious rolling readjustment this phrase would become taboo.³⁷

³⁶ Irving J. Lee, How to Talk with People (New York: Harper & Brothers, 1952), p. 95.

³⁷ John K. Galbraith, The Affluent Society (Boston: Houghton Mifflin Company, 1958), pp. 44-45.

To this quotation may also be added: "Little in language is rational. . . ." ³⁸

Is "speculator" a bad word? The following sample statements are offered in answer to the question:

Modern usage has made the term "speculator" a synonym for gambler and plunger. ³⁹

There is . . . a measure of moral opprobrium popularly linked with speculation. ⁴⁰

Speculators are naive persons who hope to use the security markets as a means of getting rich with little effort. ⁴¹

[Speaking of speculators] Living by one's wits is always somewhat contemptible. ⁴²

Speculation permits the stockholder to evade responsibility. ⁴³

Undoubtedly, the word "speculator" in the context of the stock market has acquired the connotation of "bad" in some such similar manner, as have "crisis," "panic," "depression," and "recession" in the context of business cycles. No supposition in explanation of how "speculator"

³⁸ George Santayana, Dominations and Powers (New York: Charles Scribner's Sons, 1951), p. 141.

³⁹ Baruch, p. 105.

⁴⁰ Dowrie and Fuller, p. 9.

⁴¹ Wilson E. Wright, Forecasting for Profit (New York: John Wiley and Sons, Inc., 1947), p. 122.

⁴² Lawrence L. B. Angas, Investment for Appreciation (New York: Somerset Publishing Co., 1936), p. 12.

⁴³ J. G. Hodgson, Wall Street: Asset or Liability? (New York: The H. W. Wilson Company, 1934), p. 19.

originally assumed the label of "bad" is advanced by the writer but an indication can be obtained from the "Tulipmania" and the "Bubbles" of Charles Mackay, who wrote an extensively detailed book on the delusions and madness of crowds which gives an insight into the possible reason why the word "speculator" is a "bad" word.⁴⁴ In his book, Mackay chronicled the "Tulipmania" of the Dutch which began in 1634. Both the "South Sea Bubble" of the English and the "Mississippi Bubble" of the French occurred in the early 1700's. In all three cases, the predominant impression was that of the force and extent of the crowd madness behind each of these crazes; each mania asserted itself as though an entire nation had been gripped in a hysteria of gambling.

The degree of the hysteria can be typified by the following statement by Mackay regarding the South Sea Bubble in which he lists the fantastic purposes of several joint-stock companies founded in 1720, in England, which were selling stock to the "people."

. . . but the most absurd and preposterous of all, and which showed, more completely than any other, the utter madness of the people, was one started by an unknown adventurer, entitled "a company for carrying on an undertaking of great advantage, but nobody to know what it is."⁴⁵

Each of these manias, of course, spent itself, and in the wake of each remained broken pocketbooks. As the suddenly rich became the suddenly poor, the force and energy of the crowds were shifted from desperate gambling to rage against the government and the "speculators" who provided better

⁴⁴ Charles Mackay, Memoirs of Extraordinary Popular Delusions and the Madness of Crowds (2d ed.; London: Office of the National Illustrated Library, 1852).

⁴⁵ Ibid., p. 53.

targets for the crowd's anger than the members of the crowd individually. While "everyone" was getting rich, everyone was a speculator and saw nothing wrong in speculation or speculators. But when "everyone" became poor, they were no longer speculators but "hoodwinked innocents." In the aftermath of each mania, the word "speculator" was assigned to those who, in the eyes of the crowd, had caused the mania and had remained rich at the expense of the crowd.

At the end of each mania, is there any wonder that speculators were "bad"?

Had Mackay lived in our times, he probably would have included a chapter in his book titled, "The U. S. Stock Mania of 1927-1929." Here, again, can be seen evidence of the same delusions of the crowd as previously recorded by Mackay. And the aftermath of the 1929 stock market crash produced the same transfer of crowd energy from desperate gambling to anger against the government and "speculators." Irving Fisher, in discussing the many causes assigned for the 1929 disaster, recited the following quotations which originated after the suddenly rich became the suddenly poor:

Senator Glass blames the "stock gamblers."

Congressman Clyde Kelly blames "this nation-wide gambling house which is called the New York Stock Exchange."

Senator Robinson of Arkansas blames President Hoover, Secretary Mellon and Ex-President Coolidge for their "unduly optimistic statements" about business conditions, which, he says, worked the country into a fever of speculation.

The Reverend John Haynes Holmes holds the brokers and their unholy ways responsible.

The New York Times . . . excoriates the "nation-wide army of speculators, . . ." ⁴⁶

Irving Lee said that:

. . . every expression of a man's relationship with a thing, person, or situation will involve some feeling to it, which feeling will be reflected or involved in what he says. ⁴⁷

Lee describes the feeling which can be induced from a relationship as approval, disapproval, or indifference. If approval results from some relationship, the individual uses what Lee termed "halo" words to reflect his feelings; if disapproval results, the individual relies on what Lee called "stigma" words to project his feelings into his words. In the preceding quotations from the 1929 stock market debacle, the sentiment of those quoted as regards the stock market crash certainly were reflected in their feelings of disapproval. In their choice of stigma words, we find speculators, brokers, and the New York Stock Exchange equated with gamblers, gambling house, and unholy ways. If the word "speculator" had not been classified as "bad" in the Tulipmania of the 1600's and in the Bubbles of the 1700's, it was certainly classified as such in the Stock Market Mania of 1927-1929.

Wendell Johnson noted that:

. . . the way in which we classify something determines in large measure the way in which we react to it. We classify largely by naming. Having named something, we tend to evaluate it and so to react to it in terms of the name we have given it. ⁴⁸

⁴⁶Irving Fisher, The Stock Market Crash -- and After (New York: The Macmillan Company, 1930), pp. xi-xii.

⁴⁷Lee, p. 96.

⁴⁸Johnson, p. 261.

If, through long experience, man has expressed his disapproval of various financial crazes by venting his wrath on whatever he meant by "speculator," and has classified the symbol "speculator" as bad, then by semantic inheritance there will be individuals within our society who, without experience or personal relationships, will react to "speculator" as connoting stigma. In short, speculators_n are bad because the word "speculator" is bad.

General Semantics and the Speculator

. . . man is at his best when he exercises the power of reason. To the extent that he is unreasonable — a creature of impulse, of prejudice, or rationalizations — he passes judgments and performs actions that do not comport with the realities of his environment.⁴⁹

In these words of Overstreet, does the judgment that "speculator" is bad comport with reality? Irving Lee said:

There is nothing intrinsic in a word that makes us use it for either approval or disapproval A word has a stigma—or a halo-function only when somebody uses or takes it so.⁵⁰

Therefore, the stigma of the speculator reflects only the attitudes of some individuals in our society who, by their semantic inheritance or personal experience, desire the word to reflect their disapproval.

The general semanticist, however, recognizes "speculator" as a high-order abstraction; in its use, whether as a stigma or halo word, some

⁴⁹Overstreet, The Mature Mind, p. 105.

⁵⁰Lee, p. 97.

similarities of speculators_n have been abstracted while the differences have been ignored. The term "speculator" to the general semanticist,

. . . is a verbal tent somewhere up in the stratosphere and can mean all sorts of things at lower levels, both good and bad. By itself, it means nothing.⁵¹

Both for the purposes of developing the differences in "speculator" at lower levels of abstraction and for using "speculator" as a halo word, let us consider some of the "good" associated with "speculator."

Speculation performs necessary functions:

1. It brings prices into line.
2. It promotes stability of prices.
3. It directs capital into places where it is most useful.⁵²

Speculation is a means of insurance against unescapable risks.⁵³

I have defined a speculator as a man who observes the future and acts before it occurs.⁵⁴

Deliberate, planned speculation is, in my opinion, the best and safest method to improve one's chances of preserving the purchasing power of capital or maintaining its constant convertibility into cash without loss.⁵⁵

⁵¹Stuart Chase, "Roadblocks to Understanding," Effective Communication on the Job, ed. Joseph M. Dooker (New York: American Management Association, 1956), p. 56.

⁵²Hodgson, pp. 29-30.

⁵³Ibid., p. 29.

⁵⁴Baruch, p. 105.

⁵⁵Loeb, p. 113.

Anyone who is inclined to speculate should look at speculation as a business and treat it as such and not regard it as a pure gamble as so many people are apt to do.⁵⁶

Socially, in fact, in a capitalistic community, it is highly desirable that there should exist a large body of wall-instructed speculators.⁵⁷

Thus, from another viewpoint, "speculator" is a halo word.

The general semanticist is not concerned, however, with evaluating the word as either good or bad. Since "speculation in itself may do either good or harm,"⁵⁸ he is concerned only with insuring that the emotive use of the symbol "speculator," by others, does not cause him to react emotionally to the symbol.

The general semantics approach is of significance to the investor_n in his stock market activities. The meaning he assigns to "speculator" and "investor" will have a distinct effect on his success in the stock market. If he evaluates the former as "bad" and the latter as "good," the probability is great that he will miss investment opportunities which would produce the greatest return to those not concerned with the goodness and badness of symbols. Korzybski said:

Humanity is a peculiar class of life which, in some degree, determines its own destinies; therefore in practical life words and ideas become facts -- facts, moreover, which bring about important practical consequences.⁵⁹

⁵⁶Jesse L. Livermore, How to Trade in Stocks (New York: Duell, Sloan, and Pearce, 1940), p. 5.

⁵⁷Angas, p. 12.

⁵⁸Fisher, p. 218.

⁵⁹Korzybski, Manhood of Humanity, p. 47.

Korzybski then gave the illustration of men who "have defined a stroke of lightning as being the 'punishment of God' of evil men . . .," yet other men have defined it as being simply an "electric spark." The emotive concept of the first definition prevented men from taking any action when their homes were struck by lightning for "to do so would be against the 'definition'." The practical consequence to these men was the loss of their homes. The second, nonemotive definition had the practical consequence of men providing their homes with lightning rods.⁶⁰

The investor with a multivalued, nonemotive viewpoint toward the symbols, "speculator" and "investor," enjoys the practical consequence of being free at any time to assume risk in his investments in any proportion and to any degree he judges to be correct.

⁶⁰ Ibid., pp. 47-48.

CHAPTER III

THE SEARCH FOR INVESTMENT INFORMATION

The knowledge required for successful management of capital is commonly quite foreign to the average individual's everyday activities It is imperative under these conditions that the investor have at least a realistic idea of the nature of his problem¹

--Dowrie and Fuller

We live in a world of words, which, when structured into sentences give us information which may be factual and relevant to our search for knowledge, or which may provide irrelevant or misleading information.

The decision by an investor to take specific action in the stock market is based on his judgment of the information available to him. Whether his judgment is good or bad, it cannot "be better than the information on which it is founded."² To be a successful investor implies good judgment which, in turn, requires reliable information. The obtaining of accurate information, then, is the "very crux of successful investing."³

The problems facing the investor in his search for reliable information are manifold. Initially, this chapter will consider the entropic characteristics of informational messages and the semantic noise barrier erected to distort these messages. In the latter part of the chapter,

¹Dowrie and Fuller, p. 4.

²Ibid., p. 282.

³Gilbert, p. 77.

specific examples of some of the problems encountered by the investor in his search for information and advice will be discussed.

Semantic Entropy and Noise

Claude Shannon stated that "the fundamental problem of communication is that of reproducing at one point either exactly or approximately a message selected at another point."⁴ Shannon approached this problem from the viewpoint of the engineer concerned only with the technical aspects of increasing the probability of accuracy of electronic or electrical transmission of communication symbols.⁵ The social scientist and Shannon's co-author, Warren Weaver, saw in Shannon's mathematical theory of the engineering aspects of communication a significance that transcended the pure technical aspects of communication.⁶ Weaver contended that there are three problem areas inherent in the broad subject of communication, rather than the single one implied in Shannon's writings. These three levels, according to Weaver, are:

- Level A. How accurately can the symbols of communication be transmitted?
(The technical problem.)
- Level B. How precisely do the transmitted symbols convey the desired meaning?
(The semantic problem.)
- Level C. How effectively does the received meaning affect conduct in the desired way?
(The effectiveness problem.)⁷

⁴Claude E. Shannon and Warren Weaver, The Mathematical Theory of Communication (Urbana, Ill.: The University of Illinois Press., 1949), p. 3.

⁵Chase, p. 16.

⁶Shannon and Weaver, p. 97.

⁷Ibid., p. 96.

Weaver's thesis, contrary to Shannon's contention that the "semantic aspects of communication are irrelevant to the engineering problem,"⁸ is that "the theory of Level A is, at least to a significant degree, also a theory of Levels B and C."⁹ Of significance to this paper is the relationships of the theory of Level A to Level B; Level C is concerned with behavior and thus is disregarded.

If Weaver's thesis is correct, the entropy and noise concept applied by Shannon to the technical problem of accurate communication symbol transmission can be applied also to the semantic problem of conveying precise meaning from transmitter to receiver.

Entropy is a measure of disorganization; it is the tendency of all closed systems in the universe to deteriorate and lose their distinctiveness, to move from a state of organization and differentiation toward a state of chaos and sameness.¹⁰ In communication theory, Shannon and Weaver, and Norbert Wiener advance the idea that it is possible to treat messages as having an entropy as if they were systems within the universe.¹¹ Thus, any transmitted message tends toward entropy, i.e., a message tends to lose information in the process of being transmitted and received. As Stuart Chase said:

Even the clearest message loses something in its journey, and entropy is the same for the loss. Entropy is the idea

⁸Ibid., p. 3

⁹Ibid., p. 98.

¹⁰Norbert Wiener, The Human Use of Human Beings (Garden City, New York: Doubleday & Company, Inc., 1954), p. 12.

¹¹Shannon and Weaver, pp. 18-26, and pp. 103-106; and Wiener, p. 21.

that things are running down—like a watch And now, says Shannon, like messages. There is no question about entropy [in the accurate transmitting of communication symbols] and it probably operates . . . in the transfer of meaning.¹²

Semantic entropy, then, is the tendency for the meaning of a message to be lost as the message passes from the source of information to its destination.

Using human speech as an example, the communication line begins with an information source, the brain, prepared to send out a message. The message is sent to the transmitter, the vocal system which, in turn, transmits the message by sound waves through the air. The listener's ear—the receiver—receives the sound waves and the message is transmitted to the listener's brain, the destination. The listener's brain then decodes and evaluates the message. Semantic entropy, in this case, would be the loss in the meaning of the message, as it progressed, from the meaning intended by the speaker to the meaning attached to the message by the listener.

This illustration returns us to chapter I wherein the thought was expressed that, in communicating, the individual transmitting and the individual receiving, were sharing frameworks of reference; and that each individual involved in the communication process has his own specific framework of reference, which is not the same as any other's. As Exton said:

Every man carries his own context with him. The past experience, and the character and intelligence and interests of each individual affect the meaning—the real significance to him—of what he hears or reads.¹³

¹²Chase, Power of Words, p. 19.

¹³Exton, p. 65.

To this statement may be added the observation that the speaker of words, as well as the reader of words, attaches his own context to the words he selects to symbolize as to the meaning of his message.

Thus the meaning of the message transmitted is not necessarily the meaning of the message received. This semantic entropy is the first problem faced by the investor when he attempts to derive meaning or reliable information from the intended meaning of the transmitter of the message purporting to contain information.

The second problem of the investor in his search for accurate information is the semantic "noise" which is interposed on the meaning of a message as it travels from speaker to listener. "Noise" is always mechanical in nature to the communication engineer but Chase maintained that noise "should be expanded to cover 'semantic noise,' or distortions of meaning not intended by the sender."¹⁴ This semantic noise can be likened to a barrier which is unconsciously erected by the listener which prevents him from receiving the meaning intended by the information source. And, as Kirk put it, semantic noise is always present in the communication process:

A bugaboo of communication is noise, a ghostly hand that claws at a message somewhere between source and destination, changing it into obvious nonsense or, what is worse, converting it into another meaningful but entirely misleading message. Channels are never without some noise—. . . [such as] semantic noise in the neural network of a human being trying to understand.¹⁵

¹⁴ Chase, Power of Words, p. 13.

¹⁵ John R. Kirk, "Communication Theory and Methods of Fixing Belief, Language, Meaning and Maturity, ed. Samuel I. Hayakawa (New York: Harper & Brothers, 1954), p. 113.

An example of a semantic noise barrier is found in Carl Rogers' discussion of the blocking of communication:

I would like to propose, as an hypothesis for consideration, that the major barrier to mutual interpersonal communication is our very natural tendency to judge, to evaluate, to approve or disapprove, the statement of the other person, or other group.¹⁶

Should the receiver's emotions be touched by the incoming message, his semantic noise barrier will be strengthened. As Carl Rogers continued:

Although the tendency to make evaluations is common in almost all interchanges of language, it is very much heightened in those situations where feelings and emotions are deeply involved. So the stronger our feelings, the more likely it is that there will be no mutual element in the communication. There will be just two ideas, two feelings, two judgments, missing each other in psychological space.¹⁷

An example of the truth of the latter statement of Rogers can be found in the case of an investor who holds a stock which is depressed in market price under that paid by the investor. In spite of information which indicates the price of his stock will drop even more than it already has, the investor tenaciously holds his stock in the belief that it will come back to its original price level, and thus not require him to sell at a loss. As the price of his stock continues to decrease, the investor becomes "locked-in" his investment to the point where any belated decision to sell would cause a sizeable economic loss greatly out of proportion to that which would have been sustained had he originally sold at a small loss.

¹⁶ Carl R. Rogers, "Communication: Its Blocking and Its Facilitation," Language, Meaning and Maturity, ed. Samuel I. Hayakawa (New York: Harper & Brothers, 1954), p. 54.

¹⁷ Ibid., pp. 54-55.

The investor's emotions, in this illustration, prevented him from thinking unprejudiced by his position in the stock. His sentiment against taking a loss, even though the loss initially would have been small, prevented him from making an unprejudiced assessment of his position.¹⁸ The emotional feeling against taking a loss was further fortified by his equally emotional feeling that his stock would return, in time, to its original purchase price level. And well it might, but how long will the investor have his capital "frozen" in an unprofitable investment? Would not the investor have protected his capital better had he initially sold his stock, taken a small capital loss, and reinvested in a stock that held promise for capital gain in the immediate rather than in the indefinite future?

The semantic noise barrier is not erected by the investor alone. His informational source may well induce semantic noise in the communication line in the same manner as the investor himself. The investor, then, must constantly be on guard against accepting as fact, that which is not fact. As Stuart Chase stated the problem, one of the roadblocks to understanding "is the confusion of facts with inferences or opinions or value judgments."¹⁹

To be noted at this point is the distinction which has been drawn between semantic entropy and semantic noise. The distinction is artificial in the sense that semantic noise is one of the causes of semantic entropy, i.e., it is a part of the whole. The distinction has been drawn to emphasize what is considered to be the two-fold nature of many of the informational problems facing the investor:

¹⁸ Loeb, p. 105.

¹⁹ Stuart Chase, "Roadblocks to Understanding," Effective Communication on the Job, ed. M. Joseph Dooker (New York: American Management Association, 1956), p. 53.

1. The reception of investment information with the same meaning attached by the receiver to the words of the message as intended by the transmitter.
2. The reception of investment information devoid of emotional reactions by the investor and screened by the investor to separate the facts from the opinions, emotions, and judgments of the transmitter.

Problems Encountered in the Search for Information and Advice

"Information" is a symbol which stands for the content of what an individual exchanges with the outer world as the individual adjusts to that world and makes his adjustment felt upon it.²⁰ Since an individual's personal experiences are limited to his day-to-day sphere of activity, he must of necessity turn to others for the bulk of his contact with the world outside the reach of his first-hand information. Mass media such as newspapers, periodicals, radio, and television provide the maximum of the individual's information of his outside world.

The daily newspaper, from the standpoint of volume and area of coverage, is pre-eminent among the mass media as a source of information. As important as the newspaper is in shaping our concept of the outside world, it must be recognized as the product of a highly developed abstractive process.

As an example of this abstractive process, assume that an event occurs which is observed by a reporter. The reporter culls from all his

²⁰Wiener, p. 17.

observations of the event those events which he feels are most representative. When he telephones his story in to the rewrite man, he relates what he believes to be the most significant facts concerning the event. At this stage in the development of a newspaper report of an event, we should recognize that the reporter has performed an abstraction; he has not told "all" of the event, he has told only part of it. From chapter I we know that he cannot tell all even if he desired to do so; further, since he has evaluated his observations of the event, what he selects as being most pertinent and meaningful may not necessarily be most meaningful to others.

The rewrite man selects certain of the facts and inferences of the reporter as being those which, in his judgment, will best tell a story of the event. After completing his rewrite of the reporter's story and simultaneously moving the news up another rung in the abstraction ladder, the story goes to the copy desk where it may well be shortened in the process of being checked for accuracy, etc.

Upon completion of these ascents up the abstraction ladder, the story, if it involves "policy," goes to any number of editors, who, in turn, add the editorial viewpoint to the story. The story which, even at its inception, bore slight resemblance to reality, has now gone through even higher levels of abstractions, coupled with inferences drawn from fact and includes the value judgments of nonobservers—the editors—which have been added for good measure. The surviving remnants of the original story are now subjected to the special brand of abstracting practiced by the make-up editor.

The make-up editor determines the allowable length of the story, where it shall be placed in the newspaper, and the kind of headline to use. When finally transformed into type, the story may be forced to yield to yet one more abstraction at the hands of the pressroom worker who throws out a few

lines of type if the copy will not fit into the allotted space.²¹ This mystical newspaper story has passed through a continuous process of abstraction. The facts have been distilled into the final easily read newspaper shadow story of the event. As Stuart Chase said when discussing the liabilities of mass media, "Knowledge when permitted to come through is packaged in easy capsules, to be swallowed at a gulp."²²

Perhaps this is too harsh an indictment of newspapers; possibly the fault rests in the attitude of the readers: "Says John Hersey with a fine irony: 'If we must read, we demand brevity, generous typography, mean paragraphs, philosophy that has been run through a chewing machine and been eased with editorial pepsin and bile.'"²³ Regardless of where the blame does or should rest, the fact remains that the flow of information from event to published story is not free of distortion and omissions. The newspaper, as a specific element of our communication process, is no exception to the observation of H. A. Overstreet that "in no area of our maturity . . . is arrested development more commonplace than in the area of communication."²⁴

At this point one may well ask, What has this discussion of the daily newspaper to do with the stock market? The answer is that the public has been estimated to receive as much as 90 percent of its financial

²¹ Donald M. Schwartz, "General Semantics and the Reporter's Job," Language, Meaning and Maturity, ed. Samuel I. Hayakawa (New York: Harper & Brothers, 1954), p. 140.

²² Chase, Power of Words, p. 245.

²³ Ibid.

²⁴ Overstreet, The Mature Mind, p. 54.

information from daily newspapers.²⁵ The fact that financial news is normally included in a special section of the newspaper, generally far removed from the front page, does not decrease its susceptibility to the abstractive process previously described. In fact, financial articles may well include more of the abstractive process than the conventional news story. In reporting on corporate financial events, for example, the reporter or columnist rarely, if ever, experiences these events firsthand; in most cases his story stems from an abstraction prepared by a corporate official possessing more than a nodding acquaintance with the art of public relations.

Not even the impersonal world of daily stock market statistics is capable of escaping the abstractive process of the newspaper writer. On any given trading day the action of but a handful of stocks is analyzed as if the interpretation of their action was all that was necessary to describe a day's activity in the stock market. All too often newspaper articles explaining market action are written by those who do not themselves know why the market acted as it did, but must write something to fill space and at the same time make it sound plausible.²⁶

The daily newspaper, although it may be the most popular source of financial information, is certainly not the only source of that information. The investor, whether novice or professional, will experience no difficulty in finding additional sources of information about either individual stocks or the stock market as a whole. As Clendenin said, "There is probably no other industry or type of business as abundantly supplied with trade

²⁵Douglas H. Bellemore, Investments—Principles, Practices and Analysis (New York: B. C. Forbes and Sons, Inc., 1953), p. 281.

²⁶Ibid., p. 285.

literature as is the securities business."²⁷ Examples of the diversity and volume of information may be found in any issue of The Wall Street Journal or Barron's. As a specific example, the March 5, 1962 issue of Barron's carried a total of 46 advertisements for various kinds of information on the stock market and individual stocks. This was, of course, in addition to the articles and statistical information presented by this weekly's staff and guest writers on the same subject.

The problem of the investor is not that of finding information; it is, rather, the problem of wading through the phletora of available information to find that which is meaningful and accurate.²⁸ The aspect of the abstractive process of this problem as followed in publishing a daily newspaper has already been considered. But the problem is even greater than that imposed by the process of abstracting. As examples, Dice and Eiteman pointed out some semantic noise barriers in their discussion of the art of reading the financial page:

One must be on guard . . . every minute for propaganda, crowd psychology, deliberate deception, half-truth, long-time news interpreted as representing the immediate situation, gossip, rumor, ill-advised opinion, and facts which appear adequate but in reality cover up facts of opposite import.²⁹

Even this apparently all-inclusive list of pitfalls for the unwary investor needs at least one more consideration, that is, what is published is designed to be sold. As Overstreet pointed out, in our society knowledge is something to be sold, as a commodity, to as many people as possible. With this approach, the standard governing the production of knowledge is

²⁷Clendenin, p. 273.

²⁸Baruch, pp. 261-262.

²⁹Dice and Eiteman, p. 61.

that of sales appeal rather than of accuracy and utility.³⁰ "It is not surprising, under these conditions, that information and misinformation reach the public in an undifferentiated mass . . ."³¹

Success in differentiating between sources of meaningful information and misinformation does not come to the investor over night.³² In fact, according to one successful broker-investor, G. M. Loeb, the majority of investors will never be capable of discriminating "between sources of valuable and sources of misleading information."³³ It is no wonder, then, that some investors seek help from an investment informational or advisory service.

Investment informational or advisory services can generally be classified into two broad categories according to their reporting procedures:

1. Those providing "facts as dispassionately as possible, leaving all interpretations to the investor."
2. Those providing "an analysis which offers interpretations and conclusions."³⁴

Investment services in the first category require the investor to make his own interpretations of the data presented and to arrive at his own investment decisions, accordingly. Assuming the service presents reliable facts, this approach of the individual investor making his independent

³⁰ Overstreet, The Mature Mind, p. 171.

³¹ Ibid.

³² Kamm, p. 121.

³³ Loeb, p. 53.

³⁴ Clendenin, p. 279.

analysis and decision on the basis of the service's data will probably produce the most successful investor.³⁵

Many investors, however, realize from sad experience that they lack the qualifications and/or time to manage their own investments.³⁶ Hence, the fact that they have reliable, basic data on hand is meaningless. The advisory services of the second category—those that provide interpretations and conclusions—will have an appeal for such investors. "After all, it is easier to review the conclusions of others rather than to formulate one's own."³⁷

Although there may be a variety of reasons why an investor subscribes to an advisory service of the second category, most investors subscribe "in the expectation of making speculative or investment gains from its recommendations."³⁸ Unfortunately for the expectations of the investor,

The editors of the investment literature are not so infallible that their advice can be followed without hesitation. In fact, they do not agree with each other; two leading advisory services recently published their lists of the 100 best buys chosen from the same 3,200 stocks. Only 17 stocks appeared on both lists.³⁹

Alfred Crowles, after making two studies of financial services and publications, concluded that with rare exception they had an average record that was worse than that of the average common stock over the period

³⁵Kamm, p. 122.

³⁶Bellemore, p. 305.

³⁷Clendenin, p. 279.

³⁸John Schulz, The Trend & Value Publications Prospectus (New York: WRSM Financial Service Corporation, 1961), p. 2.

³⁹Clendenin, p. 279.

studied.⁴⁰ Although note is taken of the word "average" in Crowles' conclusion, it would still appear that the investor has a formidable task in selecting the proper investment service. The general semanticist will also "date" the services that had outperformed the average stock—the successful service₁₉₄₄ may not be the successful service₁₉₆₂:

The semanticist will also note that the words "conclusions" and "recommendations" were used as if synonymous in the two preceding paragraphs. The distinction drawn between these two symbols by Schulz⁴¹ will be of academic interest to semanticists and of possible profit-and-loss interest to the investor utilizing some form of investment service.

Schulz pointed out that the conclusions presented by his investment service are the:

. . . byproducts of the process of interpretation to which we subject the material—objective as well as intangible—at our disposal. This material inevitably includes numerous variables. Its interpretation therefore becomes possible only by the exercise of judgment, which means it is fallible The resulting conclusions thus are the personal opinions of the interpreter.⁴²

Schulz added that these conclusions should not be treated as recommendations by the service subscribers. He pointed out that the conclusions of the service interpreters are valid only to the interpreters; that is, the interpreters conclude what they should do on the basis of their judgment and interpretation. But the service cannot,

⁴⁰ Alfred Crowles, "Can Stock Market Forecasters Forecast?" Econometrica, July, 1933, pp. 323-324; and "Stock Market Forecasting," Econometrica, July-October, 1944, p. 214.

⁴¹ John Schulz is a "Point and Figure" technician, a stock market academician, and an analyst for Wolfe & Company.

⁴² Schulz, p. 2.

. . . recommend what you should do, because we cannot know the numerous additional considerations—many of them subjective and personal—that you will have to superimpose on the conclusions of others in working toward your own decisions in speculations and investments.⁴³

In this excellent discourse by Schulz, the semanticist further sees the possibility of different frameworks of reference between transmitter and receiver and how semantic entropy can distort the meaning of the transmitter. And what is true and possible in the case of the specific investment service represented by John Schulz can also be true and possible in the case of any investment service.

A final point should be considered in this brief examination of the category-2 advisory service, that is, those that interpret and provide conclusions.

Statements are made from time-to-time by certain of the investment services about how they outperformed the market.⁴⁴ It would appear that an investor could solve all his investment information problems if he subscribed to the service that gave evidence of the best past record, and if he faithfully followed its advice. But the truth of this hasty conclusion is subject to at least three conditions:

1. That the investor is a "millionaire."⁴⁵
2. That, if the investor is not a "millionaire," he
can successfully superimpose his success ratio

⁴³ Ibid., p. 3.

⁴⁴ These are typically found in Barron's and The Wall Street Journal and normally stated relative to the performance of the Dow-Jones Industrial Average.

⁴⁵ The word "millionaire" is used as a symbol that the investor must be of well-above average means; not as a precise quantitative measure.

(in selecting stocks) on the success ratio of the investment service and equal the performance of the latter.

3. That the service is as successful in the future as it has been in the past.

Only the first two of these conditions will be discussed, as the third is considered to be obvious. For the discussion of the first two conditions, the investment service provided by Arnold Bernhard & Co., Inc., in its Value Line Investment Survey, is used as an example.

The Value Line Investment Survey classifies securities on which it reports into five groups and according to four attributes.⁴⁶ Group I is the "highest" group with respect to a specific attribute, and Group V is the "lowest." The attributes used by the service are:

1. Quality
2. Yield
3. Rank for Market Performance Next 12 Months
4. Rank for 3- to 5-year Appreciation Potentiality.

Thus, a particular stock may be in Group I with respect to Quality, in Group III with respect to yield, and so on. For brevity in discussion, it is assumed that an investor is interested in only one attribute, say, "Rank for Market Performance Next 12 Months."⁴⁷ Therefore, our mythical investor

⁴⁶Arnold Bernhard, The Evaluation of Common Stocks (New York: Simon Schuster, 1959), Chaps. II through IV, pp. 38-140.

⁴⁷The reader will recognize that this would not be done in actuality; the careful investor would consider all four attributes.

will be concerned only with the stocks rated in Group I with respect to that one attribute—those having the "highest" probability of favorable market performance in the next year.

The investor's first difficulty with this service will be encountered when he finds that there are approximately 160 stocks in Group I.⁴⁸ How does he select, out of 160 stocks, the number that he is capable of buying? As Bernhard was careful to point out, records of his service's performance are based on the average price performance of the entire group and "does not refer to the performance of every single stock in the group," nor does it "imply that every stock in Group I outperformed every stock in Group II, and so on down the line."⁴⁹ Therefore, unless the investor is a "millionaire," how does he buy 160 stocks to insure that he will have the same measure of success as the average of Group I?

This question is not overlooked by Bernhard. Acknowledging the impossibility of purchasing such a substantial number of stocks, he stated that the investor should diversify sufficiently to hold a representative sample and he gave 20 stocks as being a good estimate of the number required to insure about the same performance as the Group average.⁵⁰ The point that the purchase of 20 stocks does or does not require funds above the means of the "average" investor will not be argued. But Mr. Bernhard, whose entire basis for his ratings is that of statistics,⁵¹ should be reminded that as a

⁴⁸ Ibid., p. 122. The figure of 160 is the figure quoted in Bernhard's book. The number may have changed.

⁴⁹ Ibid.

⁵⁰ Ibid., pp. 129-130.

⁵¹ The word "statistics" is used in its singular sense.

statistician, he has minimized the fact that he is asking his subscribers to take a probability of a probability; that is, the subscribers are asked to superimpose their success ratio in selecting from Bernhard's 160 stocks on Bernhard's success ratio in selecting from the total of stocks under his review.

For purposes of illustrating the investor's problem of taking a probability of a probability, let us assume that Bernhard's success ratio has been 70 percent and that this ratio will continue. He therefore has a .7 probability of being right in his stock ratings. With approximately 160 stocks in Group I, he will be "right" to some degree on 112 of these stocks and "wrong" to some degree on the remaining 48. Assuming that our investor is going to diversify and has sufficient funds to purchase 20 of the total of 160 stocks in Group I, what is his probability of maintaining Bernhard's .7 probability of being right? The investor may be so fortunate as to select 20 of the 112 stocks that are going to be "right." In this event, his success ratio is 100 percent and he has outperformed Bernhard. But the investor may be highly unfortunate and select 20 of the 48 stocks that prove to be "wrong." Certainly there is more probability of selecting 20 out of the 112 good stocks than there is the probability of selecting 20 out of the 48 "bad" stocks, but there still remains some degree of risk that the investor will implement a larger percentage of incorrect selections than correct ones; in fact, regardless of how small it may be, there is always the probability that all 20 of the investor's selections from the 160 available will be "bad."

Although an investment service may provide better results for an investor than an investor may be capable of himself, it is not the

philosopher's stone which can magically transform poverty into riches.⁵²

⁵²Baruch, p. 84, with apologies for the freedom taken with his words.

CHAPTER IV

STOCK MARKET FORECASTING

. . . he was seized with a prophetic ecstasy; he danced with wild abandon, sang, jabbered inarticulate sounds, and foretold future events.¹

--Manly Palmer Hall

Premise and Arguments

Even though an investor is one of the select few who is capable of developing reliable information, he still has the problem of determining the market significance of his reliable information.²

In short, the investor must assemble facts and then make inferences from these facts. A simplified example of this process can be given as follows:

Fact: Corporation ABC's earnings for the fiscal year just ended are double those of the previous fiscal year.

Inference: The market price of ABC's stock will rise.

The fact of the earnings increase is verifiable at the instant the fact is stated or known. But the intangible of the inference is not verifiable, in the sense used here, at the instant of completion of the mental process by

¹Manly P. Hall, The Secret Teachings of All Ages (9th ed.; Los Angeles: The Philosophical Research Society Press, 1947), p. 62.

²Loeb, p. 53.

which it is made. The inference is verifiable only in the future when, in retrospect, the increase in the market price of ABC's stock proves that the inference was correct. Or the decrease in the market price of ABC's stock shows that the inference was wrong.

Whether or not the investor makes a correct decision to purchase or not to purchase ABC's stock, depends upon the value of his inference drawn from the verifiable fact. Since his inference, as used here, is concerned with the future, the investor's inference becomes a forecast of the future.

Premise: With few exceptions, e.g., the sale of stocks to settle an estate, the decision to buy, sell, or hold a stock, or do nothing, is based on a forecast that the market price of a stock is going up, down, or will hold its present price.

At least three objections to this broad statement can be advanced immediately. One argument against this premise would be the citing of an investor who invests in stock for the sole purpose of drawing income from dividends and who makes no effort to forecast the future price of his stock. If such an investor actually exists, he will either be "lucky" or else unsuccessful in his stock market operations. And this is said in the strongest sense of the Aristotelian either-or orientation.

If, after purchasing a stock, this dividend-only oriented investor decides to sell because of necessity or desire, he will be lucky if the sales price of his stock, plus dividends received, is no less than the original cost price of the stock, plus the loss or minus the gain in purchasing power of his invested funds, plus the income tax on dividends received and all charges for both the purchase and sale of his stock. He will be lucky in the sense that, as stock prices are always changing, he happened to sell at just the right time.

He has been unsuccessful if the sales price of his stock, plus dividends received, is less than the original cost price of the stock, plus the loss or minus the gain in purchasing power of his invested funds, plus the income tax on dividends received and all charges for both the purchase and sale of his stock.

The second argument against the premise would be advanced by the investor who purchases stock for either dividend income or capital appreciation, or both, based on the upward secular trend of stock prices. His argument would be that he is not required to forecast because stock prices have been advancing in a long-term upward trend at the rate of approximately $3\frac{1}{4}\%$ per year.³ Therefore, all he has to do is invest in quality stocks and "let his money ride." In the long run, he will be successful and will never be concerned with forecasting.

As a matter of fact, this investor has made at least two stock market forecasts in advancing his argument. By relying on the secular trend to insure that stock prices, in the long run, will go up, he has rendered a forecast; that is, he has made a forecast based on past action. By asserting his capability of picking quality stocks, he must be forecasting that, in the indefinite future, the price of these stocks will not go down or, if they do go down, they will eventually come back up to a point at least equalling their purchase price.

And this investor should also realize that he is forecasting that he has patience and, further, that he can maintain an unemotional attitude toward market price fluctuations. Certainly the investor who purchased

³Dice and Eiteman, pp. 233-234.

stocks at or near the high of the Dow-Jones Industrial Average in 1929 had to exercise considerable patience and an unemotional attitude as he waited a quarter of a century for the Industrial Average to return to the point where it was when he made his purchases.

The third argument against the premise can be raised by citing the various formula plans that promise stock market profit without forecasting. An excellent example of the absurdity of this belief is found in a book with the appropriate title, Stock Market Profit without Forecasting.⁴ In the introduction to this book, the author, Edgar Genstein, stated: "Formula plans involve no forecasting . . .," and two sentences later, ". . . it is implicitly assumed by any formula plan that there will be substantial upward and downward movements in stock prices in the future, just as there has been in the past."⁵ Is not the implicit assumption of the future a forecast of the future?

Possibly the equating of an implicit assumption with a forecast is too tenuous to prove the absurdity. Not tenuous, however, are the "buy" and "sell" signals given by the author's formula plan.⁶ First, singling out the author's "buy" signal for scrutiny, what is a "buy" signal other than a recommendation to buy a stock? And why buy if the stock price is not expected to rise? Does it not follow that a "buy" signal is a forecast of rising prices? Second, when does the investor following Genstein's formula sell? He sells when the formula gives the "sell" signal. And,

⁴Edgar S. Genstein, Stock Market Profit without Forecasting (Larchmont, New York: American Research Council, 1956).

⁵Ibid., pp. 2-3.

⁶Ibid., pp. 24-63.

according to the author, his nonforecasting formula gives the signal to sell when stocks are over-priced; in other words, when stock prices can be expected to drop. Is this not forecasting?

Genstein's formula does not help the investor select a particular stock—the formula determines only the time to buy and sell based solely on the market as measured by the Dow-Jones Industrial Average.⁷ The investor thus retains the residual problem of determining what stock should be bought after Genstein's formula says "buy." And the problem of determining the stock to be bought takes us back to the beginning where the investor, whether he likes it or not, has to make a forecast.

Completion of this side-excursion brings us back to the original premise that, with few exceptions, the investor bases his investment decisions on a forecast.

Two Aspects of Stock Market Forecasts

Whether the investor makes his own forecasts or relies on the forecasts of others, he is confronted with the fact that these predictions deal with probabilities on two variable planes, that is, "price" and "time."⁸ The first, price, is concerned with forecasting that the price of a stock or the value of a market index is going up, down, or will hold relatively steady. A price forecast may involve setting a definite price goal or it may be given in broader terms, which is more common, that the price is going up or down but with no definite quantitative measure of the price movement being given. The second variable, time, is nebulous and is rarely

⁷Ibid., pp. 24-63. One exception pointed out by Genstein where his formula worked with an individual stock was in the case of the American Telephone and Telegraph.

⁸Schulz, p. 3.

identified when considering stock market forecasts; in fact, it is rarely referred to. If, for example, a definite price goal is forecast for a stock, it is common for the forecaster to ignore the time when this price goal should be reached. Or, if the price forecast is given in nonquantitative terms, no forecast is given for the period of time within which the price movement is expected.

The nebulous character of "time" when applied to stock market forecasting was well brought out by Daniel Seligman in his series on personal investing in Fortune.⁹ Seligman, in discussing point and figure chartists, brought up the question of how long should a prediction remain unfulfilled before the forecaster should acknowledge that he was wrong. Edmund Tabell¹⁰ answered, ". . . no time limit could be put on a target's fulfillment."¹¹ Seligman continued:

Schulz¹² is especially mysterious on this subject. "Price targets," he has written, "may generally be presumed to imply a degree of probability that the price level they identify will, in due course, be reached."¹³

To paraphrase Seligman, all we have to do now is define "due course."

Mackay, writing about the prophecies of Nostradamus, made an observation pertinent to the "time" aspect of stock market forecasting:

⁹Daniel Seligman, "The Mystique of Point and Figure," Fortune, March, 1962, p. 113.

¹⁰Edmund Tabell is head of institutional research for, and a partner of, Walston & Co. His weekly market letter has a circulation of 30,000.

¹¹Seligman, p. 113.

¹²See reference to Schulz in Chap. III, supra.

¹³Seligman, p. 113.

[The prophecies of Nostradamus] take so great a latitude, both as to time and space, that they are almost sure to be fulfilled somewhere or other in the course of a few centuries. A little ingenuity . . . might easily make events to fit some of them.¹⁴

Mackay also discussed the English astrologer, Lilly, who attempted to convince the House of Commons that he had foretold the great fire of London. Lilly maintained that he had forecast the fire in his Monarchy or no Monarchy "in the form of an hieroglyphical plate representing on one side a large city in flames—. . . "

"Did you foresee the year of the fire?" said a member.

"No" quoth Lilly, "nor was I desirous. Of that I made no scrutiny."¹⁵

The element of time seems to be as much a problem to our modern day stock market forecasters as to the prophets of old. In general, it is ignored now as it was centuries ago.

Forecasting Methods

Nebulous as the time aspect of forecasting may be, it is still necessary that the investor, if he desires to be successful, attempt to determine the correct time to buy and sell. There are many different methods in use for forecasting market and stock prices. The two major classifications which include the majority of all methods, with the exception of those based on intuition and astrology,¹⁶ are commonly referred to as the fundamental,

¹⁴Mackay, p. 247.

¹⁵Ibid., p. 245.

¹⁶Wilson E. Wright, Forecasting for Profit (New York: B. C. Forbes and Sons Publishing Co., Inc., 1953), p. 102. Wright mentioned an occasion when he investigated an advisory service and found that its "recommendations were based on the movement of the planets."

and the technical.¹⁷ The fundamentalists are investors "who try to foresee the future by analyzing financial and operating data about the company . . ."¹⁸
According to Edwards and Magee:

The stock market fundamentalist depends on statistics. He examines the auditors' reports, the profit-and-loss statements, the quarterly balance sheets, the dividend records and policies of the companies whose shares he has under observation. He analyzes sales data, managerial ability, plant capacity, the competition. He turns to bank and treasury reports, production indexes, price statistics and crop forecasts to gauge the state of business in general, and reads the daily news carefully to arrive at an estimate of future business conditions. Taking all these things into account, he evaluates his stock; if it is selling currently below his appraisal he regards it as a buy.¹⁹

The technicians, on the other hand, are investors "who try to foresee the future by analyzing the behavior of the stock itself. Technicians are usually chartists, . . ."²⁰ Edwards and Magee, who are chartist-technicians, defined technical analysis as follows:

The term technical in its application to the stock market has come to have a very special meaning, quite different from its ordinary dictionary definition. It refers to the study of the action of the market itself as opposed to the study of the goods in which the market deals. Technical Analysis is the science of recording, usually in graphic form, the actual history of trading (price changes, volume of transactions, etc.) in a certain stock or in "the averages" and then deducing from that pictured history the probable future trend.²¹

¹⁷Edwards and Magee, p. 3.

¹⁸Seligman, p. 113.

¹⁹Edwards and Magee, p. 3.

²⁰Seligman, p. 113.

²¹Edwards and Magee, p. 5.

As might be expected from the stated definitions of fundamentalist and technician, there have developed two opposing schools of thought as to which is the correct or best method to use. In reading the literature, it seems as though one is re-reading the arguments for and against speculating and investing. Dice and Eiteman, for example, pointed out that the most successful investors are those who follow the fundamental approach.²² Edwards and Magee disagreed and pointed out that the charts of the technician "are far more prescient than the best informed and most shrewd . . ." of the fundamentalists.²³

The technicians and the fundamentalists, however, cut across the boundaries of the speculator-investor controversy. For example, Bernard Baruch, a speculator, used the fundamental approach to his investments.²⁴ G. M. Loeb, another speculator, uses the technical approach to his stock market operations.²⁵

Also similar to the speculator-investor controversy is the "bad-good" word connotation for technician-fundamentalist. As Schulz pointed out, fundamental analysis "has attained a certain academic standing, while technical analysis has not . . ." ²⁶ A possible explanation for the attachment of a stigma connotation to "technician" is given by Seligman:

²²Dice and Eiteman, pp. 226-227.

²³Edwards and Magee, p. 6.

²⁴Baruch, pp. 256-257.

²⁵Loeb, p. 68.

²⁶Schulz, p. 4.

A chartist is, to begin with, a technician Charting was generally in bad odor during the 1920's and early 1930's. It was associated with stock manipulations--i.e., the manipulators kept charts of price and volume activity, looking for ways to control the prices of stocks on minimal investments; at the same time a few traders tried to use charts in an effort to detect manipulations. Aside from these shady connotations, there was always a widespread suspicion that the chartists were all a little crazy.²⁷

Over the years, however, "the charting of stocks, once a recondite art practiced only by a few Wall Streeters, is becoming the recondite pre-occupation of masses of investors."²⁸ Apparently the acceptance of the technician and his charting approach by greater numbers of nonprofessional investors has erased much of the original stigma. This change was attested to by Seligman when he said: "It is apparent that charting has now become respectable."²⁹

The multivalued approach to the symbols, "technician" and "fundamental," recognizes that both deal with certain variables and intangibles that are inherent in any type of forecasting. Both deal with probabilities and both require inferences to be drawn from information which, hopefully, is free of semantic noise and has not suffered from semantic entropy. The general semanticist recognizes that neither approach to forecasting "can ever achieve complete success . . ."³⁰ As Schulz said:

There are . . . aspects of technical analysis with which fundamental analysis cannot compete, just as there are aspects

²⁷ Daniel Seligman, "Playing the Market with Charts," Fortune, February, 1962, p. 118.

²⁸ Ibid.

²⁹ Ibid.

³⁰ Schulz, p. 4.

of fundamental analysis into which the technical approach cannot penetrate. There is thus every reason for supplementing the one approach with the other, and no reason whatever to use either of them to the exclusion of the other as the sole basis for decisions in investment and speculation.³¹

Attitude Toward Forecasting

The perfect forecaster would have to know all there was to know about a particular stock. But as indicated in chapter I, no one can know all about anything. The investor, therefore, should not waste either his time or money in searching for the perfect forecasting method, for none exists.

Peter Drucker, in discussing management decision-making, made a statement which directly applies to the investor making an investment decision based on a forecast where all is not known and never will be known:

The manager [investor] will never be able to get all the facts he should have. Most decisions have to be based on incomplete knowledge-- . . . To make a sound decision, it is not necessary to have all the facts; but it is necessary to know what information is lacking in order to judge how much of a risk the decision involves.³²

The investor must be aware of the abstractive nature of a forecast. Since he cannot, nor can anyone else, know all there is to know about a stock, what he does know is an abstraction from the total of reality. The parts of the whole that have been neglected in the investor's abstractive process may well have as great an effect on his forecast as those parts abstracted.³³

³¹ Ibid.

³² Peter F. Drucker, The Practice of Management (New York: Harper & Brothers, 1954).

³³ Lee, p. 64.

Another problem involved in the abstractive process of forecasting was stated by Wright:

The time spent studying abstract situations involving many variables may produce a state of mind in which many answers may be conceived to almost any problem--there being no single choice upon which action can be taken. Anything becomes possible, and nothing is probable.³⁴

The investor should further attempt to separate himself from emotional reactions when attempting to forecast stock price movements. As Baruch said:

My years in Wall Street . . . became one long course of education in human nature. Nearly always the problem that arose in the Stock Exchange . . . was how to disentangle the impersonal facts of a situation from the elements of human psychology which came with these facts.³⁵

This separation of the investor from his emotions is a worthy objective, but for the average investor it is virtually impossible. In discussing the weathervane type of advisory service that fluctuates in its advice in keeping with current conditions, Kamm observed:

. . . this same variation in philosophy is typical of the average investor. When things look pessimistic, he feels that way. When conditions look optimistic, he feels optimistic.³⁶

In short, the forecaster-investor "possesses only human images and concepts His knowledge is an ideal figment . . . dramatized by his private

³⁴Wright, p. 6.

³⁵Baruch, p. ix.

³⁶Kamm, p. 126.

passions."³⁷ In view of these obstacles to forecasting, it is no wonder that one attitude toward predicting stock prices is that of simply disregarding forecasting and forecasters "on the ground that no prophet can be 'completely certain,' . . ."³⁸ But the more desirable attitude for the investor is that stated by Wright:

A second attitude implies . . . a recognition that the fallibility of prophets is not something unusual, A full consciousness on our part that prophets . . . abstract from the totality will prevent despair and cynicism on the one hand and disappointment on the other. Prophecies must be looked upon not as infallible truths but as possible guides and hints of what probably will happen.³⁹

The investor must assume that every forecast contains an error. The important consideration is not that the forecast contains an error, but "the magnitude and direction of the error."⁴⁰

³⁷Santayana, Dominations and Powers, p. 188.

³⁸Wright, p. 65.

³⁹Ibid.

⁴⁰Ibid., p. 13.

CHAPTER V

STOCK MARKET SUCCESS

Many have the greed but not the talent.

--Unknown

What is Success in the Stock Market?

The Aristotelian dichotomy recognizes man as being either a success or a failure. But man may succeed in one endeavor and fail in another. What, then, is he, a success or a failure?

If man strives for success in the absolute, Aristotelian two-valued sense, it will forever elude him. It eludes him, as Wendell Johnson pointed out, because absolute success does not exist—"it is a verbal mirage."

What he seeks to escape is an absolute failure, what he anxiously pursues is an absolute success—and they do not exist outside his aching head. What he does in fact achieve is a series of relative successes; and these are all that he, these are all that anyone, can ever achieve.¹

As we strive to go, from what can be referred to generally as "failure," to something else which can be evaluated as "success," the crucial point, according to Johnson, is "that one which we agree to recognize as the point of transition—the point at which we leave failure and enter success;

¹Johnson, pp. 5-6.

Unless such a point can be recognized, we are denied the experience of believing that we have reached our destination, that we have achieved "success." And until we can believe that we have achieved "success," we continue to assume that we have not achieved it—we continue to experience "failure." Under such circumstances we feel frustrated, and, eventually, distraught.²

The non-Aristotelian investor recognizes that he cannot always be right in his stock investments. He hopes to be right more often than he is wrong. But if he fails to cut his losses when he has made a wrong stock selection and fails to let his profits ride when he has made a right stock selection, he can be successful in terms of selecting more right stocks than wrong and yet be a failure in terms of money lost.³ Thus, we can conclude that, while it is desirable for an investor to have as his goal the selection of more right stocks than wrong stocks, for this gives a greater probability of success, financial success does not necessarily follow from stock selection success.

It thus appears that the failure-success transition point of Johnson, when applied to the stock market, is that point where the investor is capable of maintaining the purchasing power of his funds. If the investor cannot maintain the purchasing power of his funds, he is a failure. If he maintains or betters the purchasing power of his funds, he is a success. It is not sufficient to measure success in terms of numbers of dollars, as was well illustrated by Frank Vanderlip:

²Ibid., pp. 4-5.

³Edwards and Magee, pp. 420-421; Livermore, pp. 11-13; and Loeb, pp. 103-108; 118-119; and 123.

[Vanderlip] showed that if an investor had placed \$1,000 in a savings bank in 1900 and had allowed it to accumulate at compound interest, he would have had \$2,000 in 1920. However according to Mr. Vanderlip's calculations, the investor would have had to add from his pocket another \$1,000 in order to buy exactly as many goods as he could have purchased during 1900 with the original \$1,000 deposit.⁴

To which may be added Loeb's comment concerning the difficulty in maintaining purchasing power:

. . . should some super-solvent agency agree to preserve the buying power of capital for a substantial length of time at a stated fee per annum, informed people would embrace the plan enthusiastically if they felt there was any real possibility of the agency staying solvent.⁵

The Obstacle to Stock Market Riches

Most books written on the subject of the stock market offer the reader a list of principles or rules, or advance a plan or a theory on how to invest.⁶ Since none of these are particularly difficult to understand, then why the paucity of investors who have become wealthy due to their stock market activities? Perhaps some plausible reasons why all stock investors are not wealthy are contained in this statement by Kamm:

Success in the stock market requires knowledge and experience and both of these come slowly. When once acquired and combined with certain requisite personal characteristics,⁷ they open the way to material increases in income and wealth.

⁴Frank A. Vanderlip, Saturday Evening Post, January, 1933; quoted from Loeb, p. 19.

⁵Loeb, p. 19.

⁶Examples, by no means all-inclusive, include: Angas, pp. 5-6; Baruch, p. 254; Bellemore, pp. 393-410; Clendenin, pp. 662-663; Dice and Enteman, pp. 414-434; Dowrie and Fuller, pp. 587-589; Kamm, pp. 65-89; Livermore, pp. 81-90; and Loeb, p. 116.

⁷Kamm, p. 4.

Kamm made three points in his statement:

1. The investor must possess knowledge.
2. The investor must have experience.
3. The preceding two must be combined with certain requisite personal characteristics.

It is the writer's thesis that the primary reason why there are so few wealthy stock market investors is that, while the first two of Kamm's requirements for success can be acquired, the third cannot. We may assume that intelligence and knowledge can be acquired; that even a small amount of capital, stock market experience can be acquired; but as for the third point,

. . . making money in the market demands a lot of "genius" or "flair." No amount of study or practice can make one successful in the handling of capital if one really is not cut out for it.⁸

To which should be added the following statement by Humphrey Neill:

Money-making is a mental characteristic. It is my personal belief that it is an exceedingly difficult art to acquire; that, indeed, one is born with it. You have an acquisitive nature (I believe), or you haven't . . . Education has little or nothing to do with the money-making characteristic.⁹

Is the flair of Loeb or Neill's premise of the existence of a "money-mind" so alien to our way of thinking? This is doubted, for a ". . . key value in our culture is the belief that each individual is endowed with certain unique gifts, talents, and potentialities . . ."¹⁰

⁸ Loeb, p. 14.

⁹ Humphrey B. Neill, The Art of Contrary Thinking (Caldwell, Idaho: The Caxton Printers, Ltd., 1956), p. 105.

¹⁰ O. A. Ohmann, "Search for a Managerial Philosophy," Harvard Business Review, September-October, 1957, p. 47.

Overstreet, in propounding his maturity concept, stated that one "insight of modern psychology is the idea of individual uniqueness." If an investor does not possess the unique characteristic of what has been termed a "money-mind," and is, consequently, unsuccessful on the stock market,

. . . he may blame himself for the low level of his accomplishment or his persistent discontent; but not all his self-berating, nor even all his efforts to become more competent by further training, can make up for the original aptitude-lack.¹¹

Conclusion

Any way one looks at it, nothing is more difficult than succeeding in Wall Street, yet nothing is attempted by such poorly equipped people or is considered as easy.¹²

¹¹Overstreet, The Mature Mind, pp. 32-33.

¹²Loeb, p. 15.

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